FILE COPY

Office-Supreme Court, U. S.
FILED
JAN 30 1951

IN THE

Supreme Court of the United States

OCTOBER TERM, 1950

No. 526

THELMA D. PARR and GEORGE B. PARR,
Petitioners,

versus

FRANK SCOFIELD, Individually and as United States Collector of Internal Revenue,
Respondent.

PETITION FOR WRIT OF CERTIORARI AND BRIEF IN SUPPORT THEREOF

THELMA D. PARR AND GEORGE B. PARR
By:
J. B. Lewright,
Bedell Building,
San Antonio, Texas.
Attorney for Petitioners.

MUCKLEROY MCDONNOLD
Transit Tower
San Antonio, Texas
Of Counsel

AMERICAN PRINTERS

SUBJECT INDEX

	Page
Petition for writ of certiorari	1-6
Summary statement of the matter involved	1-4
Basis upon which this Court has jurisdiction	4
Questions presented	4
Reasons for the allowance of the writ	5
Prayer for the writ	5
Brief in support of petition for writ of certiorari	7-17
Opinions of the courts below	7
Grounds on which jurisdiction is invoked	7
Statutes involved	8
Statement of the case	8
Specification of errors	8
Argument	9-17
Summary of argument	9
Point 1	9
Point 2	12
Point 3	15
Conclusion	18

TABLE OF CASES CITED

Blair v. Commissioner, 300 U. S. 5 15

Farrell v. Commissioner, 134 F. (2d) 193 12

First Mechanics Bank of Trenton, N. J., et al v. Commissioner, 91 F. (2d) 275 ..... 5, 9, 13

Foran v. Commissioner, 165 F. (2d) 705 12

Freuler v. Helvering, 291 U. S. 35 15

Grace Bros. v. Commissioner, 173 F. (2d) 170 12

Hamill & Smith v. Parr, 173 S. W. (2d) 725 ..... 5, 10

Helvering v. Armstrong, 69 F. (2d) 370 ..... 5, 12

Helvering v. Stuart, 317 U. S. 154 15

Kirby Petroleum Co. v. Commissioner, 326 U. S. 599 ..... 5, 9, 15

Lyeth v. Hoey, 305 U. S. 188 15

Magruder v. Supplee, 316 U. S. 394 15

Massey v. Commissioner, 143 F. (2d) 429, 431 16

McMurray v. Reynolds, 38 F. (2d) 480 10

Reynolds v. McMurray, 60. F. (2d) 843, cert. denied 287 U. S. 644 ..... 5, 9, 11, 12

U. S. v. Ogilvie Hardware Co., Inc., 330 U. S. 709 15

TABLE OF STATUTES CITED

Internal Revenue Code:

Sec. 23 (m) (26 U. S. C. 1946 ed., Sec. 23) 4, 5, 8, 9

Sec. 114 (b) (3) (26 U. S. C., 1946 ed., Sec. 114) 3, 6, 8, 9

Sec. 182 (c) (26 U. S. C., 1946 ed., Sec. 182) 4, 9, 13

Sec. 3801 (b) (3) (26 U.S.C., 1946 ed., Sec. 3801 15

IN THE

Supreme Court of the United States

OCTOBER TERM, 1950

No.———————

THELMA D. PARR and GEORGE B. PARR,
Petitioners,

versus

FRANK SCOFIELD, Individually and as United States Collector of Internal Revenue,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

TO THE HONORABLE FRED M. VINSON, CHIEF JUSTICE OF THE UNITED STATES AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Your petitioners respectfully show:

I.

SUMMARY STATEMENT OF THE MATTER INVOLVED

This is an action under the Tucker Act to recover income taxes and interest alleged to have been illegally assessed and collected for the year 1944.

During the year 1936, George B. Parr acquired as community property a 420-acre oil and gas lease in Webb County, Texas, hereinafter sometimes called the Benavides Lease, and in the same year transferred the lease to Hamill & Smith, a partnership, (Stip. of Facts, R. 15, 16), retaining equitable title to one-fourth of said lease. (Plaintiffs' Exhibit 2, R. 34, 51, 61). At the time of the transfer to Hamill & Smih, there was an oral agreement that Hamill & Smith would take care of the financing and would develop and operate such lease for the mutual benefit of George B. Parr and Hamill & Smith. (Plaintiffs' Exhibit 2, R. 34, 51, 53, 88, 89). After production was obtained under the lease, Hamill & Smith disputed the existence of the agreement, and Parr brought suit against them in the state court. Parr assigned 45% of his interest in the property and accumulated income to his lawyers. The suit was ultimately decided in Parr's favor, and he was adjudged to possess a one-fourth interest in the lease and equipment, and to be entitled to be reimbursed for his one-fourth of the profits earned in the prior years, as well as to receive a similar portion of the profits earned in the future, (R. 89), with proper adjustment for the disbursements made by Hamill & Smith for Parr's one-fourth of the equipment, and the sum of $10,000.00 previously paid to Parr. (Plaintiffs' Exhibit 2, R. 34, 51, 62).

The judgment became final in January of 1944, and Hamill & Smith accounted for Parr's one-fourth of the net income from the beginning of operations in 1936 to December 31, 1943. (Stip. of Facts, R. 15, 17).

As a result of the suit, Parr received the following sums of money from Hamill & Smith during the year 1944:

55% of 25% of net income from the lease	$165,554.30
55% of 25% of interest allowed on the judgment	22,868.58
Total	$188,422.88

(R. 89).

In 1945, Parr and his wife filed separate returns for the year 1944, in which they reported one-fourth of the net income from the 1944 operations of the lease. They did not report any income from the lease attributable to operations prior to 1944; but they filed amended returns for the years 1940 to 1943, inclusive, in which they reported their distributive share of net income from the lease. During the year 1945, they filed delinquent partnership income tax returns in the name of Hamill & Smith & Parr for the years 1936 to 1943, inclusive. (R. 89, 90).

Upon examination of petitioners' 1944 income tax returns, the Commissioner found that the amount collected on the state court judgment, plus the fair market value of petitioners' interest in the lease and equipment, constituted income from litigation for the year 1944 not subject to any depletion allowance. As a result of this finding, the Commissioner assessed additional taxes and interest against George B. Parr and Thelma D. Parr in the respective amounts of $93,219.40 and $93,370.06. Petitioners paid the additional assessments, and then filed claims for refund, which were rejected. Then they filed this suit in the district court to recover the amounts alleged to be illegally assessed against them. The district court denied recovery, holding that the taxpayers were required to report in 1944, as income, the sums recovered by them in 1944 in the state court. In so holding, the court rejected the taxpayers' contention that, because Parr was a member of a partnership, the income should have

been taxed in the years when earned, as well as their contention that they were entitled to a deduction for depletion under Section 23(m) of the Internal Revenue Code. (R. 90).

The petitioners appealed to the Fifth U. S. Circuit Court of Appeals, and that court affirmed the judgment of the district court. (R. 88-93).

II.

BASIS UPON WHICH THIS COURT HAS JURISDICTION

The judgment of the Circuit Court of Appeals was entered on December 7, 1950. This Court has jurisdiction under Section 1254(1), Title 28, United States Code, Judiciary and Judicial Procedure, and Supreme Court Rule No. 38, Section 5.

III.

QUESTIONS PRESENTED

1. Was George B. Parr a joint adventurer with the partnership of Hamill & Smith for the years 1936 to 1943, inclusive?

2. If George B. Parr was a joint adventurer with Hamill & Smith for the years 1936 to 1943, inclusive, did the fact that such relationship had to be established by litigation remove the case from the operation of Section 182(c), Internal Revenue Code, which requires a joint adventurer (partner) to report his distributive share of partnership income, whether or not distribution is made to him?

3. If, under the law and facts of this case, George B. Parr was required to report in his 1944 return his

share of net income earned for the years 1936 to 1943, inclusive, was he entitled to a deduction for depletion on his share of gross income from an oil producing lease under Sections 23(m) and 114(b)(3) of the Internal Revenue Code?

IV.

REASONS RELIED ON FOR THE ALLOWANCE OF THE WRIT

1. In holding that the relationship between Hamill & Smith and Parr did not constitute a joint venture, the courts below arrived at a conclusion of law in direct conflict with the decisions of the Tenth Circuit Court of Appeals in *Reynolds* v. *McMurray*, 60 F.(2d) 843, cert. denied, 287 U. S. 664; the Ninth Circuit Court of Appeals in *Helvering* v. *Armstrong*, 69 F.(2d) 370; and the Civil Court of Appeals for the Fourth Supreme Judicial District of Texas in *Hamill & Smith* v. *Parr*, 173 S. W. (2d) 725.

2. The decision of said Circuit Court of Appeals that Parr would not be entitled to a recovery, even if he had been able to establish a partnership or joint venture, is in direct conflict with the decision of the Third Circuit Court of Appeals in *First Mechanics Bank of Trenton* v. *Commissioner*, 91 F. (2d) 275.

3. The decisions of the courts below that petitioners are not entitled to a deduction for percentage depletion are in direct conflict with the decision of this Court in *Kirby Petroleum Co.* v. *Commissioner*, 326 U. S. 599.

Wherefore, your petitioners pray that a writ of certiorari issue under the seal of this Court, directed to the Circuit Court of Appeals for the Fifth Circuit, commanding said court to certify and send to this Court a full and

complete transcript of the record and of the proceedings of the said Circuit Court had in the case numbered and entitled on its docket, No. 13,160, THELMA D. PARR and GEORGE B. PARR, Appellants, v. FRANK SCOFIELD, Appellee, to the end that this cause may be reviewed and determined by this Court as provided for by the statutes of the United States; and that the judgment herein of said Circuit Court be reversed by the Court, and for such further relief as to this Court may seem proper.

THELMA D. PARR AND GEORGE B. PARR

By:_____
J. B. Lewright,
Bedell Building,
San Antonio, Texas.
Attorney for Petitioners.

MUCKLEROY MCDONNOLD
Transit Tower
San Antonio, Texas
Of Counsel

IN THE

Supreme Court of the United States

OCTOBER TERM, 1950

No.————————

THELMA D. PARR and GEORGE B. PARR,
Petitioners,

versus

FRANK SCOFIELD, Individually and as United States Collector of Internal Revenue,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OR CERTIORARI

I.

OPINIONS OF THE COURTS BELOW

The opinion in the distict court (R. 65) is reported in 89 F. Supp. 98. The opinion in the Circuit Court of Appeals (R. 88-92) is reported in ..... F. (2d) .....

II.

GROUNDS ON WHICH JURISDICTION IS INVOKED

The jurisdiction of this Court is invoked under Section 1254(1) Title 28, United States Code, Judiciary

and Judicial Procedure, and under Supreme Court Rule No. 38, Sec. 5.

III.

STATUTES INVOLVED

The applicable statutes will be found in the Appendix, *infra.*

IV.

STATEMENT OF THE CASE

This has already been stated in the preceding petition under I (pp. 1-4), which is hereby adopted and made a part of this brief.

V.

SPECIFICATION OF ERRORS

The Circuit Court of Appeals erred in holding:

1. That George B. Parr was not a joint adventurer with the partnership of Hamill & Smith for the years 1936 to 1943, inclusive.

2. That even if George B. Parr was a joint adventurer with Hamill & Smith for the years 1936 to 1943, inclusive, he was not taxable on his share of net income until he received it in 1944.

3. That George B. Parr was not entitled to a deduction for depletion on his share of gross income from the Benavides Lease under Sections 23(m) and 114(b)(3), Internal Revenue Code.

VI.

ARGUMENT

SUMMARY OF THE ARGUMENT

POINT 1. Petitioners established by the stipulation of facts (Plaintiffs' Exhibit 1, R. 15-21) and the judgment of a state court (Plaintiffs' Exhibit 2, R. 34, 51-65) the existence of a joint venture between the partnership of Hamill & Smith and George B. Parr for the years 1936 to 1943, inclusive. *Reynolds* v. *McMurray*, 60 F. (2d) 843, cert. denied, 287 U. S. 664.

POINT 2. Having established that George B. Parr was a joint adventurer with Hamill & Smith for the years 1936 to 1943, inclusive, petitioners were taxable on their distributive share of net income from the joint venture in the years in which earned. Sec. 182 (a), Internal Revenue Code; *First Mechanics Bank of Trenton* vs. *Commissioner*, 91 F. (2d) 275.

POINT 3. Having established under state law their ownership of a one-fourth interest in the Benavides Lease from the date of acquisition, (Plaintiffs' Exhibit 2, R. 34, 51, 61), petitioners had an economic interest in the oil and gas in place that was depleted by production, and they are entitled to percentage depletion under Sections 23 (m) and 114 (b) (3) of the Internal Revenue Code. *Kirby Petroleum Co.* v. *Commissioner*, 326 U. S. 599.

POINT 1.

The respondent offered no evidence in the trial court to show that George B. Parr was not a joint adventurer with Hamill & Smith during the years in question. On the other hand, petitioners introduced in evidence, as part of the stipulations of fact, their sworn statements setting out facts sufficient to establish the joint venture. (R. 15,

22-31). In addition, they introduced in evidence the verdict of the jury and the judgment of the state district court entered in the suit alleged in their claims for refund. The jury found as a fact that Hamill & Smith agreed to take care of the financing and to develop and operate said lease for the mutual benefit of George B. Parr and Hamill & Smith. (Plaintiffs' Exhibit 2, R. 34, 51, 53). The judgment of said state court recited that Hamill & Smith had made disbursements for themselves and George B. Parr in the drilling, development and operation of said lease, and that the income from said lease had been received by Hamill & Smith for themselves and George B. Parr. (Plaintiffs' Exhibit 2, R. 34, 51, 62).

On appeal by Hamill & Smith from the judgment of the state district court to the Fourth Civil Court of Appeals, said Civil Court of Appeals held that Parr was a joint adventurer with Hamill & Smith. *Hamill & Smith* v. *Parr*, 173 S. W. 2d 725.

In *McMurray* v. *Reynolds*, 38 F. (2d) 480, McMurray owned an interest in a prospective oil field, having acquired the same through one Armstrong. Sometime prior to the year for which additional income taxes were assessed against McMurray, an agreement for the promotion and development of the oil field was entered into with an oil company, under which agreement the company was to advance all the funds necessary for the promotion and development of the property, and that such expense would be borne solely by the company, unless oil or gas was produced. Upon the happening of such contingency, however, the expense of such promotion and development would be borne upon the basis of 60 per cent to the company and 40 per cent to Armstrong, and that said 40 per cent of such expense should be charged upon the books of the company against Armstrong until it, together with

the 60 per cent borne by the developing company, should liquidate the entire cost of the development. The development of the property proceeded, resulting in the discovery of oil, and the arrangement between the parties was carried into effect by the company, charging Armstrong with his 40 per cent of the development and crediting his account with his 40 per cent of the proceeds from production. The condition so prevailed in 1920, concerning which the first controversy over income taxes arose, that a considerable portion of the product from the oil field had been marketed, but not a sufficient amount to cover the expense of the development.

McMurray, owner of a portion of the original Armstrong interest, did not report any income from the property for the year 1920. The Bureau assessed additional taxes for the year 1920 against McMurray on the theory that he had to report his share of income from the joint venture. McMurray paid the taxes under protest, then brought suit in the district court to recover. The district court entered judgment for the taxpayer and an appeal followed. The Tenth Circuit Court of Appeals reversed, holding that the parties were joint adventurers and the income from the oil property was the income of both joint adventurers. *Reynolds* v. *McMurray*, 60. F. (2d) 843. The Supreme Court denied certiorari, 287 U. S. 664.

The principal arguments of the respondent on this point in the courts below were that Hamill & Smith had not agreed to be joint adventurers with Parr, and that Parr did not participate in the management or in the operation of the property. The argument that Hamill & Smith did not agree to the joint venture is refuted by the verdict and judgment in the state court. The argument that a joint venture can not exist unless all joint adventurers participate in the management or in the operation of the

business is without merit and is refuted by the decision of the Tenth Circuit Court of Appeals in *Reynolds* v. *Mcmurray*, 60 F. (2d) 843, and by the decision of the Ninth Circuit Court of Appeals in *Helvering* v. *Armstrong*, 69 F. (2d) 370.

The Circuit Court of Appeals in the instant case, citing *Farrell* v. *Commissioner*, 134 F. (2d) 193, held that the essential issue concerning the existence of an asserted joint venture was a question of fact for decision by the trial court, and that it was not convinced that the decision of the trial court was clearly erroneous. Petitioners concede that the issue of a joint venture was a question of fact for decision by the trial court, but petitioners submit that, since there is not a scintilla of evidence in the record rebutting petitioners' proof that there was a joint venture, the decision of the trial court on this issue was clearly erroneous as a matter of law. *Foran* v. *Commissioner*, 165 F. (2d) 705; *Grace Bros.* v. *Commissioner*, 173 F. (2d) 170.

The facts as to the issue of a joint venture, as determined by the judgment of the state court, are on all fours with those in *Reynolds* v. *McMurray*, 60 F. (2d) 843, and the decisions of the courts below are in direct conflict therewith. This Court should resolve the conflict.

POINT 2.

The Circuit Court of Appeals, again citing *Farrell* v. *Commissioner*, 134 F. (2d) 193, held that even if Parr was a joint adventurer with Hamill & Smith for the years 1936 to 1943, inclusive, he was not taxable on his share of partnership income until he received it in 1944. It is respectfully submitted that the *Farrell* case is no authority for this proposition. In the *Farrell* case, the court specifically held that there was no partnership or joint venture.

Petitioners concede that they are not taxable until 1944 on their share of income from the Benavides Lease unless George B. Parr was a joint adventurer with Hamill & Smith. If this Court holds that there was a joint venture with Hamill & Smith, then petitioners are taxable on their distributive share of partnership income in the years in which the income was earned. (Sec. 182(a), Internal Revenue Code). The decision of the Circuit Court of Appeals to the contrary is in direct conflict with the decision of the Third Circuit Court of Appeals in *First Mechanics Bank of Trenton, N. J., et al* v. *Commissioner*, 91 F. (2d) 275, in which case one J. Philip Bird and the Canadian Car & Foundry Company, Ltd., hereinafter called the Canadian Company, were joint adventurers in manufacturing munitions for the Imperial Russian Government. One contract was completed in the year 1916 and certain profits were realized by the joint adventurers. There was no claim by the Canadian Company that Bird was not entitled to any portion of the profits, but it did deny that he was entitled to the amount claimed by Bird. Litigation followed and sometime after October 22, 1922, Bird obtained judgment in the sum of $312,723.46. The Canadian Company appealed to the Kings Bench of Canada. Before the appeal was heard, however, the Canadian Company and Bird reached an agreement in 1928 whereby Bird accepted $200,000 as a compromise settlement.

In his income tax report for 1928, Bird reported the net amount of his profits from the joint venture as capital gain and paid $20,646.22 thereon. The Commissioner of Internal Revenue assessed a deficiency of $20,179.53 against Bird on the ground that his net profit constituted ordinary net income for the year 1928 and that Bird was an employee and not a joint adventurer. Bird appealed to the Board of Tax Appeals contending that the income,

if any, was received, within the meaning of the Revenue Acts, in 1916 and not in 1928. Bird died before the appeal was heard and his executors were substituted as the petitioners.

The Board sustained the Commissioner and the petitioners appealed to the U. S. Circuit Court of Appeals for the Third Circuit. That Honorable Court held that the relationship between Bird and the Canadian Company was a joint venture and that Bird was taxable on his distributive share of the net profits for the year 1916. The Court said:

> "In the present case the contracts were completed in 1916. The profits were realized by the joint venture at that time and there was nothing conditional or contingent about their receipt. They were earned and paid. Bird, therefore, was legally entitled to his share of the profits which was $312,723.46, and was taxable on that share although he did not actually receive it in that year. That he saw fit to compromise the amount due him for $200,000 in 1928 did not diminish his liability for taxes for 1916. * * *
>
> "In the case at bar, the fact that a controversy arose between the joint venturers did not change the fact that profits, taxable income, had been received in 1916 by the partnership."

It is respectfully submitted that the decisions of the courts below are in conflict with the decision of the Third Circuit Court of Appeals and this Court should exercise jurisdiction to resolve the conflict.

The attention of this Court is called to the fact that the Commissioner may reopen any of petitioners' prior

years in which they have failed to report their distributive share of partnership income from the Benavides Lease. (Section 3801 (b) (3), I. R. C.). Therefore, the Federal government will not lose any revenue to which it is entitled in the event that it is held that a partner is taxable on his distributive share of partnership income for the year in which earned, even though the partnership agreement has to be established by litigation. Section 3801 was inserted in the Revenue Act of 1938 to cover situations of this kind.

POINT 3.

The decision of the state court holding that Parr owned a one-fourth interest in the Benavides Lease from date of acquisition in 1936, is an adjudication of property rights under state law and is binding on the Commissioner and the Federal government. *U. S.* v. *Ogilvie Hardware Co., Inc.*, 330 U. S. 709; *Helvering* v. *Stuart*, 317 U. S. 154; *Magruder* v. *Supplee*, 316 U. S. 394; *Lyeth* v. *Hoey*, 305 U. S. 188; *Blair* v. *Commissioner*, 300 U. S. 5; *Freuler* v. *Helvering*, 291 U. S. 35. When Parr took title to the lease in his own name, he held legal title thereto but Hamill & Smith owned equitable title to three-fourths of the lease. When Parr transferred legal title to the lease to Hamill & Smith, he retained equitable title to one-fourth thereof. Thereafter, Parr had an economic interest in the oil in place that was depleted by production. In *Kirby Petroleum Co.* v. *Commissioner*, 326 U. S. 599, this Court held that if a taxpayer had an economic interest in oil and gas in place that was depleted by production, he was entitled to depletion on income from the property, even though he did not hold title to the property. It is respectfully submitted that petitioners are entitled to depletion on their share of gross income from the property under the doctrine of *Kirby Petroleum Co.* v. *Commissioner*, *su-*

pra, and that the courts below committed reversible error in holding to the contrary.

The argument of respondent that petitioners realized income from litigation rather than from the Benavides Lease is pure sophistry. Parr recovered one-fourth of the gross income from the lease, less one-fourth of the disbursements made by Hamill and Smith for the benefit of themselves and Parr.

The Circuit Court of Appeals said:

> "The appellants are entitled to no depletion deduction, because they had no known, established, or legally recognized interest until the litigation in the state court was determined."

It may, perhaps, suffice to call this Court's attention to the fact that the foregoing statement ignores the decision of the state court wherein it was held that Parr owned a one-fourth interest in the lease from the date of acquisition, but petitioners would further show that the one case cited to support the reasoning of the Circuit Court of Appeals, *Massey* v. *Commissioner*, 143 F. (2d) 429, 431, does not do so. In the *Massey* case, one Massey, an attorney, contracted to represent a client for an interest in an oil and gas lease. The Fifth Circuit Court of Appeals correctly held that Massey was not entitled to depletion on oil produced prior to the time he acquired his interest in the lease. Massey was in the same position with respect to depletion as Parr's attorneys would be if they claimed depletion on the oil produced prior to August 1, 1941, the date they received an assignment to 45% of Parr's interest in the lease and accumulated income. In this case, Parr acquired legal title to the lease in 1936, he then transferred legal title to Hamill & Smith but retained equitable title to one-fourth of said lease. The fact that he had to bring suit to es-

tablish his legal title did not change the fact that he had equitable title, a depletable interest, to one-fourth of the oil in place from the date of acquisition in 1936. According to the reasoning of the Circuit Court of Appeals, if Hamill & Smith had given Parr a valid written assignment of the one-fourth interest in the lease in 1936, but Parr had misplaced the written assignment before recording it, and Hamill & Smith had then denied having made the assignment until several years later when Parr found the misplaced instrument and brought suit and recovered his share of income from the lease, Parr would not be entitled to depletion because he would have had "no known, established, or legally recognized interest until the litigation was determined."

The Circuit Court of Appeals further held that petitioners were not entitled to depletion because Hamill & Smith were required to report the entire income from the property as their taxable income, and were entitled to depletion thereon. It is significant that no authorities were cited to support this theory. If any other court has ever held that one taxpayer is required to report another taxpayers' income in his own return, the petitioners have been unable to locate such decision. Neither do the petitioners know of any other decision where a taxpayer has been denied depletion on his income from oil because some other taxpayer had either mistakenly or intentionally reported the same income.

CONCLUSION

It is respectfully submitted that this case is one calling for the exercise by this Court of its supervisory powers, by granting a writ of certiorari and thereafter reviewing and reversing said decision.

THELMA D. PARR AND GEORGE B. PARR

By:_____
J. B. Lewright,
Bedell Building,
San Antonio, Texas.
Attorney for Petitioners.

MUCKLEROY MCDONNOLD
Transit Tower
San Antonio, Texas
Of Counsel

APPENDIX

INTERNAL REVENUE CODE:

Sec. 182. TAX OF PARTNERS. In computing the net income of each partner, he shall include, whether or not distribution is made to him—

(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, * * *

Sec. 3797 (a) (2). PARTNERSHIP AND PARTNER. The term "partnership" includes a syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation or venture is carried on, and which is not, within the meaning of this title, a trust or estate or a corporation; and the term "partner" includes a member in such a syndicate, group, pool, joint venture, or organization.

Sec. 23. DEDUCTIONS FROM GROSS INCOME. In computing net income there shall be allowed as deductions: * * *

(m) DEPLETION. In the case of * * * oil and gas wells, * * * a reasonable allowance for depletion * * *.

Sec. 114 (b) (3). PERCENTAGE DEPLETION FOR OIL AND GAS WELLS. In the case of oil and gas wells the allowance for depletion under Section 23 (m) shall be 27½ per centum of the gross income from the property during the taxable year * * *. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property * * *.

Sec. 3801. MITIGATION OF EFFECT OF LIMITATION AND OTHER PROVISIONS IN INCOME TAX CASES.

(a) DEFINITIONS. For the purpose of this section—

(3) RELATED TAXPAYER. The term "related taxpayer" means a taxpayer who, with the taxpayer with respect to whom a determination specified in subsection (b) (1), (2), (3), or (4) is made, stood in the taxable year with respect to which the erroneous * * * exclusion * * * therein referred to was made, in one of the following relationships: * * * (F) partner.

(b) CIRCUMSTANCES OF ADJUSTMENT. When a determination under the income tax laws—

(3) Requires the exclusion from grass income of an item with respect to which tax was paid and which was erroneously excluded or omitted from the gross income of the taxpayer for another taxable year or from the gross income of a related taxpayer, * * * and, on the date the determination becomes final, correction of the effect of the error is prevented by the operation (whether before, or after May 28, 1938) of any provision of the internal revenue laws other than this section and other than section 3761 (relating to compromises), then the effect of the error shall be corrected by an adjustment made under this section * * *.

(c) METHOD OF ADJUSTMENT. The adjustment authorized in subsection (b) shall be made by assessing and collecting * * * the amount thereof * * * in the same manner as if it were a deficiency * * *.

INDEX

	Page
Opinions below	1
Jurisdiction	1
Questions presented	2
Statutes involved	3
Statement	5
Argument	8
Conclusion	16

CITATIONS

Cases:

Balestrieri, Joe, & Co. v. *Commissioner*, 177 F. 2d 867	9
Burton-Sutton Oil Co. v. *Commissioner*, 328 U. S. 25	12
Commissioner v. *Culbertson*, 337 U. S. 733	8
Commissioner v. *Tower*, 327 U. S. 280	8
Farrell v. *Commissioner*, 134 F. 2d 193, certiorari denied, 320 U. S. 745	8, 13
First Mechanics Bank v. *Commissioner*, 91 F. 2d 275	13
Gardner v. *Wesner*, 55 S.W. 2d 1104	10
Hamill & Smith v. *Parr*, 173 S. W. 2d 725	11, 12
Helvering v. *Armstrong*, 69 F. 2d 370	11, 12, 13
Helvering v. *Bankline Oil Co.*, 303 U. S. 362	15
Johnson v. *Murray Co.*, 90 S. W. 2d 920	10
Kirby Petroleum Co. v. *Commissioner*, 326 U. S. 599	12, 15
Luling Oil & Gas Co. v. *Humble Oil & Ref. Co.*, 144 Tex. 475	10
Lusthaus v. *Commissioner*, 327 U. S. 293	8
Massey v. *Commissioner*, 143 F. 2d 429	15
North American Oil v. *Burnet*, 286 U. S. 417	14
Porter v. *Cooke*, 127 F. 2d 853, certiorari denied, 317 U. S. 670	10
Reynolds v. *McMurray*, 60 F. 2d 843, certiorari denied, 287 U. S. 664	11, 12, 13
Transcontinental Oil Co. v. *Mid-Kansas Oil & Gas Co.*, 29 F. 2d 323	10
United States v. *Lewis*, No. 347	14
United States v. *Safety Car Heating Co.*, 297 U. S. 88	14

Statutes:

Internal Revenue Code:

	Page
Sec. 23 (26 U.S.C., 1946 ed., Sec. 23)	3
Sec. 114 (26 U.S.C. 1946 ed., Sec. 114)	3
Sec. 182 (26 U.S.C. 1946 ed., Sec. 182)	4, 14
Sec. 3797 (26 U.S.C. 1946 ed., Sec. 3797)	4, 9, 10

Miscellaneous:

G.C.M. 22730, 1941-1 Cum. Bull. 214	12

Federal Rules of Civil Procedure:

Rule 52(a)	11

In the Supreme Court of the United States

OCTOBER TERM, 1950

No. 526

THELMA D. PARR AND GEORGE B. PARR, PETITIONERS

v.

FRANK SCOFIELD, INDIVIDUALLY AND AS UNITED STATES COLLECTOR OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and conclusions of law of the District Court (R. 66-74) are reported in 89 F. Supp. 98. Its memorandum opinion (R. 65) is not reported. The opinion of the Court of Appeals (R. 87-90) is reported at 185 F. 2d 535.

JURISDICTION

The judgment of the Court of Appeals was entered on December 7, 1950 (R. 90). The petition

for a writ of certiorari was filed on January 30, 1951. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254.

QUESTIONS PRESENTED

1. Whether the Court of Appeals erred in holding that the finding of the District Court that taxpayer was not a joint venturer with Hamill & Smith, a partnership, in the development and operation of an oil and gas lease was not clearly erroneous.

2. Whether, on the assumption, contrary to the finding, that taxpayer was a joint venturer in the operation of the lease, the Court of Appeals erred in holding that taxpayer was taxable in any event in 1944 upon the entire amount received in that year pursuant to a judgment awarding him a one-fourth interest in the lease and equipment thereon, and in the net profits therefrom, from the beginning of operations in 1936 to the date of judgment on December 23, 1942.

3. Whether, under Sections 23 (m) and 114 (b)(3) of the Internal Revenue Code, the taxpayer is entitled to a deduction for depletion in 1944 on the amount of net profits received pursuant to the judgment.

STATUTES INVOLVED

Internal Revenue Code:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(m) *Depletion.*—In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner, with the approval of the Secretary. * * *

* * * * *

(26 U. S. C. 1946 ed., Sec. 23.)

SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

* * * * *

(b) *Basis for Depletion.*—

* * * * *

(3) *Percentage Depletion for Oil and Gas Wells.*—In the case of oil and gas wells the allowance for depletion under Section 23(m) shall be 27½ per centum of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the

property. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance under section 23(m) be less than it would be if computed without reference to this paragraph.

* * * * *

(26 U. S. C. 1946 ed., Sec. 114.)

SEC. 182. TAX OF PARTNERS.

In computing the net income of each partner, he shall include, whether or not distribution is made to him—

* * * * *

(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183(b).

(26 U. S. C. 1946 ed., Sec. 182.)

SEC. 3797. DEFINITIONS.

(a) When used in this title, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof—

* * * * *

(2) *Partnership and Partner.*—The term "partnership" includes a syndicate, group, pool, joint venture, or other unincorporated organization, through or by means of which any business, financial operation, or venture is carried on, and which is not, within the

meaning of this title, a trust or estate or a corporation; and the term "partner" includes a member in such a syndicate, group, pool, joint venture, or organization.

* * * * *

(26 U. S. C. 1946 ed., Sec. 3797.)

STATEMENT

The facts as found by the district court may be summarized as follows:

In 1936, the taxpayer [1] acquired an oil and gas lease in Webb County, Texas, and thereafter transferred the lease to Hamill & Smith, a partnership. Hamill & Smith proceeded to develop and equip the lease, without any participation by the taxpayer. After production was had on the property, the taxpayer claimed that, by oral agreement, he had retained a one-fourth interest in the lease and equipment, and that Hamill & Smith were to reimburse themselves for the taxpayer's one-fourth of the costs and expenses, and were to pay over to him the net income from his interest. Hamill & Smith denied the existence of this agreement. In 1941, the taxpayer instituted suit against them in the Texas courts to recover an "undivided

[1] The consolidated cases involve as taxpayers George B. Parr and his former wife, the income in question having been reported in their separate returns as community property income. For convenience, however, George B. Parr will be referred to as the taxpayer. Since institution of the suits, George B. Parr and Thelma D. Parr have been divorced (R. 76), and are proceeding individually herein.

¼ interest" in the lease and "one-fourth of the profits realized from such" lease. (R. 66-67.)

The taxpayer secured a verdict in the state court, by virtue of which he was awarded an undivided one-fourth interest in the lease and equipment, and one-fourth of the net income from the property from the inception of operations in 1936 to the date of judgment. (R. 59-64.)

After the judgment became final, Hamill & Smith, during February 1944, paid to the taxpayer all funds due under the judgment, together with interest. As a result of the suit, the taxpayer, who had previously assigned a 45 percent interest in the property and the net income to his attorneys, received the following amounts (R. 68):

55% of 25% of net income from the lease—	$165,554.30
55% of 25% (*sic*) of interest allowed on judgment	22,868.58
Total	$188,422.88

Prior to 1944, Hamill & Smith never recognized the taxpayer's claim to an interest in the lease and they reported all the income and expenses of the lease in their income tax returns for those years. (R. 68-69.)

Prior to 1945, the taxpayer did not report any part of the net profits from the lease nor were returns filed prior to 1945 reflecting the existence of an alleged joint venture consisting of taxpayer

and Hamill & Smith. In that year, the taxpayer filed amended returns for the years 1942 and 1943, and included therein one-fourth of the net profits derived from the operation of the lease in each of those years, and paid the additional taxes disclosed on the amended returns. Also, in 1945, the taxpayer filed partnership returns in the name of Hamill & Smith & Parr for the years 1936 to 1943, setting forth the distributable income derived from the operation of the lease in those years. The taxpayer, however, has never reported for tax any part of his net income derived from the operation of the lease from 1936 to 1941, inclusive. (R. 69-70.)

The filing in the year 1945 of partnership returns for prior years was at the suggestion of taxpayer's counsel. The partnership of Hamill & Smith did not know at that time and, so far as the record discloses, did not know at the date of trial that such returns had been filed. (R. 70.)

The Commissioner determined that there should have been included in the taxpayer's 1944 return the amount of income and the fair market value of the lease and equipment acquired by him as a result of the judgment. Consequently, additional amounts of tax were assessed for that year against the taxpayer and his wife. These amounts were paid and the Commissioner rejected timely claims for refund which had been filed. The refund claims alleged that the taxpayer was a member of

a joint venture and that the income was taxable to him in the years when earned by the joint venture, and not in the year of receipt. Alternatively, it was alleged that the taxpayer was entitled to a deduction for depletion with respect to the income received. (R. 70-72.)

Thereafter, the taxpayer and his wife instituted suit to recover the taxes which were alleged to have been erroneously overpaid for the year 1944. (R. 2-10.) The district court decided that the taxpayer and his wife had not overpaid their taxes and dismissed the complaint. (R. 74-76.) On appeal from the dismissal of the complaint, the Court of Appeals for the Fifth Circuit affirmed. (R. 87-90.)

ARGUMENT

1. Whether the taxpayer and Hamill & Smith intended to become joint venturers is a question of fact. *Commissioner* v. *Culbertson,* 337 U. S. 733, 741; *Commissioner* v. *Tower,* 327 U. S. 280, 287; *Lusthaus* v. *Commissioner,* 327 U. S. 293; *Farrell* v. *Commissioner,* 134 F. 2d 193 (C. A. 5), certiorari denied, 320 U. S. 745. The district court found that they were not joint venturers (R. 72), and the court below held that the district court's finding was not clearly erroneous. In so holding, the court below was plainly right.

The fee title to the lease was transferred, without reservation (R. 16, 67), to Hamill & Smith and remained in them until the termination of litiga-

tion in the state court pertaining thereto, in 1944, and the judgment of the Texas district court for Webb County (R. 17, 61-63) was simply that the taxpayer owned a one-fourth interest in the lease and equipment and had a right to receive from Hamill & Smith, the operators of the lease, one-fourth of their net profits from the operation. Hamill & Smith, at all times prior to the time the state court judgment became final, denied that there was a joint venture between them and taxpayer, or that taxpayer had any interest in the lease (R. 18, 67, 69, 72). Taxpayer took no part in the operation or development of the enterprise (R. 41, 67, 72). Hamill & Smith furnished all of the capital for the enterprise (R. 16, 35, 52). In the circumstances, and since taxpayer's equitable interest in the lease was retained, the district court could properly infer that his interest never became a part of the property which the other alleged joint venturers had acquired and exposed to the risks of the business. The district court could also properly infer that taxpayer had no personal liability for the debts of the business, a usual condition precedent to a joint venture. *Joe Balestrieri & Co.* v. *Commissioner*, 177 F. 2d 867 (C. A. 9).

Moreover, it is obvious that Hamill & Smith never intended to enter into the alleged venture with taxpayer, since they never filed partnership tax returns covering it [2] (R. 18). A joint venture

[2] Section 3797(a)(2) of the Internal Revenue Code includes a joint venture within the definition of a partnership.

cannot exist unless the parties intend to associate in that capacity. *Luling Oil & Gas Co.* v. *Humble Oil & Ref. Co.*, 144 Tex. 475, 483-484; *Porter* v. *Cooke*, 127 F. 2d 853, 857-858 (C. A. 5), certiorari denied, 317 U. S. 670. Cf. *Commissioner* v. *Culbertson, supra.* Indeed, taxpayer's suit against Hamill & Smith was not premised on the contention that he was a joint venturer with them (R. 17), and apparently he never asserted that there was such an alleged joint venture until the belated partnership returns were filed by him in 1945 (R. 18-19).

Taxpayer's arrangement with Hamill & Smith was no more than a sublease, with the rent measured by a stated portion of the sublessee's net profits, *i.e.*, he permitted them to use his fractional interest in the lease in consideration for their paying him one-fourth of the net profits and their giving him a fractional interest in the equipment. Thus, there was an abundance of evidence to support the district court's finding that there was no joint venture between taxpayer and Hamill & Smith, within the meaning of Section 3797(a)(2) of the Internal Revenue Code, *supra*, pp. 4-5, or under the local law. See *Luling Oil & Gas Co.* v. *Humble Oil & Ref. Co., supra*, 144 Tex. 475; *Johnson* v. *Murray Co.*, 90 S. W. 2d 920, 923 (Tex. Civ. App.); *Gardner* v. *Wesner*, 55 S. W. 2d 1104 (Tex. Civ. App.). Cf. *Transcontinental Oil Co.* v. *Mid-Kansas Oil & Gas Co.*, 29 F. 2d 323 (C. A. 5).

Plainly, then, the court below did not err in refusing to disturb the finding of the district court that there was no joint venture between taxpayer and Hamill & Smith. See Rule 52(a), F. R. C. P. Petitioners concede (Br. 13) that if there was no joint venture, they were taxable in 1944 on the entire amount awarded by the judgment of the state court.

2. Petitioners' contention (Pet. 5, Br. 9-12) that the decision of the court below is in conflict with *Hamill & Smith* v. *Parr*, 173 S. W. 2d 725 (Tex. Civ App.); *Reynolds* v. *McMurray*, 60 F. 2d 843 (C. A. 10), certiorari denied, 287 U. S. 664; and *Helvering* v. *Armstrong*, 69 F. 2d 370 (C. A. 9), is without merit.

(a) The judgment of the court below approving the district court's finding is not in conflict with *Hamill & Smith* v. *Parr*, 173 S. W. 2d 725 (Tex. Civ. App.). Taxpayer's suit in the Texas court was not based on any theory of a joint venture and there was no allegation that one existed. The findings of the jury (R. 52-59) do not suggest the existence of a joint venture. The judgment of the state trial court was not based on the theory that one existed. (R. 51-64.) The same is true of the decision of the Court of Civil Appeals, with respect to which taxpayer alleges a conflict. The only reference in the appellate court's opinion to a joint venture was with respect only to the procurement

of the lease, not with respect to operations thereunder. *Hamill & Smith* v. *Parr*, 173 S. W. 2d 725, 727, *supra*.

Nor is the decision below in conflict with *Reynolds* v. *McMurray* and *Helvering* v. *Armstrong*, *supra*.[3] Both of those cases arose out of the same leases and agreements, and the facts were dissimilar to those presented in the instant case. There the agreements were not contested and no litigation was necessary to settle questions of title and accounting. Moreover, the agreements provided that the accounting should be made for the proportionate part of the oil and gas produced, not the net proceeds. And in those cases the primary question was whether the advances made by the operating party for capital expenditures were income to the non-operating parties. In the *McMurray* case, the Tenth Circuit held that in the circumstances the non-operating interests could be in receipt of taxable income even where there was no net income payable. Although the court described the parties as joint adventurers, it is clear that the court there was not speaking in terms of a joint venture which would be treated as a partnership for tax purposes, and was not holding that the parties were required

---

[3] In G.C.M. 22730, 1941-1 Cum. Bull. 214, 223-224, the Bureau of Internal Revenue repudiated the "joint venture" theory which it had taken in the *McMurray* and *Armstrong* cases. The tax result actually reached in those decisions is, moreover, contrary to the decisions of this Court in *Kirby Petroleum Co.* v. *Commissioner*, 326 U.S. 599, and in *Burton-Sutton Oil Co.* v. *Commissioner*, 328 U.S. 25.

to file partnership returns and be taxed as partners. As indicated, the question presented and decided in the *McMurray* and *Armstrong* cases (the Ninth Circuit in the *Armstrong* case followed the reasoning of the Tenth Circuit in the *McMurray* case.) was quite different from the issue here.

b. The decision below does not conflict, as taxpayer asserts (Pet. 5, Br. 13), with *First Mechanics Bank* v. *Commissioner,* 91 F. 2d 275 (C.A. 3), in holding that taxpayer was not taxable until 1944 on the part of the lease profits paid to him in 1944, even if he be considered a joint venturer. In that case there was no dispute between the parties respecting their relationship, it having been conceded that the taxpayer was a partner, entitled to a share of the firm profits; the only matter in dispute was as to the amount due him. Here taxpayer's right to any part of the lease profits was contested and was not determined until termination of the litigation. Taxpayer received nothing until 1944 and he was then taxable on the full amount, since he reported income on the cash basis of accounting. See *Farrell* v. *Commissioner, supra,* 134 F. 2d at p. 194. Thus, in the case at bar, where it was unknown whether the taxpayer had any rights at all under the lease until the termination of the litigation in the state court, the court below held that the taxpayer's income in question did not derive from the lease but was recovered by litigation. In the *Mechanics Bank* case, on the other hand,

where there was no contest over title to the lease, but only a dispute over the accounting, the court held that the income in question derived from the lease and the joint venture. The distinction between the two cases is clear.

The holding of the court below that the taxpayer's income was recovered by litigation is, of course, plainly correct. Section 182 of the Internal Revenue Code, *supra*, p. 4, in requiring a partner to include in his taxable income his distributive share of partnership earnings, regardless of whether or not distribution is actually made, has no reference to a mere claim to earnings where the very existence of the partnership or joint venture is in dispute. Taxpayer had no right to any property or earnings during the time that Hamill & Smith were actually contesting his claim. Consequently, taxpayer was not a partner entitled to a distributive share of partnership earnings which could be reported as his income under Section 182 until termination of the litigation. Decisions of this Court make it clear that taxpayer had no income until the dispute was settled, and similarly Hamill & Smith were taxable on all of the income in prior years as received under a claim of right and could deduct the amount paid to taxpayer in 1944. *North American Oil* v. *Burnet*, 286 U.S. 417; *United States* v. *Safety Car Heating Co.*, 297 U.S. 88; see the Government's brief in *United States* v. *Lewis*, No. 347, now pending before this Court.

3. The holding of the court below (R. 90) that taxpayer is not entitled to a deduction for depletion on the amount, representing his share of past net profits, received in 1944, does not conflict, as taxpayer asserts (Pet. 5), with *Kirby Petroleum Co.* v. *Commissioner,* 326 U.S. 599. Taxpayer here had no economic interest in oil and gas which was depleted by production until after the litigation was terminated in his favor. His depletable interest in the property and net profits was first established by the judgment of the state court, and he became entitled to depletion only with respect to production from the property after that time. The amount paid by Hamill & Smith as equal to a part of the past profits earned before taxpayer's interest in the property was established did not represent, as to taxpayer, proceeds or profits from the production of oil but rather merely payment of a money judgment. *Massey* v. *Commissioner,* 143 F. 2d 429, 431 (C.A. 5). Cf. *Helvering* v. *Bankline Oil Co.,* 303 U.S. 362, 367.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

PHILIP B. PERLMAN,
Solicitor General.

THERON LAMAR CAUDLE,
Assistant Attorney General.

ELLIS N. SLACK,
HELEN GOODNER,
EDWARD J. P. ZIMMERMAN,
Special Assistants to the Attorney General,

JOHN R. BENNEY,
Attorney.

MARCH, 1951.

☆ U. S. GOVERNMENT PRINTING OFFICE: 1951 935773 608